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INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION

OF THE

PRESIDENT

TO THE

EXECUTIVE DIRECTORS

ON A

PROPOSED CREDIT

TO THE

REPUBLIC OF KOREA

FOR

TECHNICAL ASSISTANCE

AND ENGINEERING

STUDIES

FOR

HIGHWAYS

July 3, 1968

INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION OF THE PRESIDENT TO THE
EXECUTIVE DIRECTORS ON A PROPOSED CREDIT TO THE
REPUBLIC OF KOREA FOR TECHNICAL ASSISTANCE
AND ENGINEERING STUDIES FOR HIGHWAYS

1. I submit the following report and recommendation on a proposed credit in an amount in various currencies equivalent to US\$3.5 million to the Republic of Korea.

PART I - HISTORICAL

2. In 1965, the Bank made a technical assistance grant for a comprehensive survey of all modes of transportation in the Republic of Korea. The survey report drew attention to the lack of adequate roads and recommended that the Government devote more attention to road development. The report also recommended major changes in the organization of highway administration, planning, construction and maintenance, together with provision for transport coordination.

3. In March 1967, the Government asked IDA for assistance in carrying out highway feasibility studies. Having obtained UNDP's reaction that it could not consider assistance for the highway program because of other commitments in Korea, an IDA mission went to Korea to discuss the roads to be covered by the proposed studies and the preliminary draft terms of reference for consultants. The Government agreed with IDA's proposals to study a number of specific high priority roads totalling 1,160 Km. and to provide assistance in highway organization and transport coordination.

4. Negotiations in connection with the proposed credit took place in Washington between May 23 and June 13, 1968. The Government was represented by Mr. Hak So Kim, Director, Bureau of Planning, Ministry of Construction; Mr. Sung Yong Wei of the Economic Planning Board and Mr. Hong Wo Nam, Second Secretary, Embassy of Korea.

5. The proposed IDA credit would be the third to Korea. It would be in line with the Bank Group's strategy in Korea, to help relieve bottlenecks to economic development. One of the major bottlenecks is the lack of adequate transport facilities, of which highways is the most serious. This technical assistance credit is expected to result in substantial improvement of the road network.

The following is a summary statement of Bank loans and IDA credits to Korea as of May 31, 1968:

<u>Loan or Credit No.</u>	<u>Year</u>	<u>Borrower</u>	<u>Purpose</u>	<u>Amount (U.S. \$ million)</u>		
				<u>Bank</u>	<u>IDA</u>	<u>Undisbursed</u>
25	1962	Republic of Korea	Railroad		13.9	Nil
110	1967	Republic of Korea	Second Railway		11.0	11.0
529	1968	Korea Development Finance Corpora- tion (KDFC)	Industry	5.0		5.0
Total (less cancellations) now out- standing and held by Bank and IDA				<u>5.0</u>	<u>24.9</u>	<u> </u>
Total undisbursed				<u>5.0</u>	<u>11.0</u>	<u>16.0</u>

There have been no major problems with the above projects. Disbursements under Credit No. 110 have only just started as they are dependent on the manufacture and shipment of freight cars to the borrower. Within this fiscal year I expect to present for your approval a railway, an irrigation and an education project.

PART II - DESCRIPTION OF THE PROPOSED CREDIT

7. Borrower: Republic of Korea.
- Amount: The equivalent in various currencies of \$3.5 million.
- Purpose: To cover the foreign exchange costs of highway feasibility, organization and detailed engineering studies and overseas training.
- Amortization: The credit is to be repaid over a period of 12 years including a grace period of 4 years. Amortization will be in 16 semi-annual instalments commencing November 1, 1972 and ending May 1, 1980.
- Service Charge: 3/4 of 1% per annum.

PART III - THE PROJECT

8. An appraisal report entitled "Proposal for a Technical Assistance and Engineering Credit for Highways, Republic of Korea" (TO-642a) dated July 1, 1968, is attached. The project consists of consultant studies to review the present highway administration and transport coordination

agencies, and the provision of technical assistance to implement the recommendations of the consultants; feasibility and engineering studies on selected roads; and the provision of funds for training overseas of selected Korean personnel.

9. There are about 34,000 Km. of public roads in Korea, of which less than 6 percent are paved. The existing roads are narrow, poorly aligned, badly surfaced and inadequately drained. They cannot meet the needs of an economy which has been growing rapidly in recent years, with industrial output increasing at about 20 percent annually. The project includes feasibility studies of 1,160 Km. of national highways, selected and agreed with the Government as being of high priority, including traffic forecasts and reconnaissance field surveys, recommendations for design standards and alignment selection, and an initial economic analysis for all the roads. Of these, about 800 Km. of high priority roads would be selected for more detailed field surveys, preliminary engineering and a more comprehensive economic analysis. On the basis of the feasibility studies, detailed engineering would be undertaken for sections of roads of highest priority, totalling between 300 and 500 Km.

10. In the past Korea has relied primarily on railways for transportation. With rapid economic growth, demand for a wider range of transport services has arisen, including the roads now being planned. This demand for a wider range of transport services also gives rise to the need for coordination of transport investment, and pricing and regulatory policies to ensure that resources devoted to transport are used efficiently. Under the project, the present responsibilities of ministries and other agencies concerned with transportation policy would be examined and recommendations would be made for appropriate changes including the establishment of a transport coordination organization.

11. Highway functions are at present dispersed among several ministries and the various Provincial Governments, resulting in weak financial control and confused responsibilities and lines of authority. Construction funds are channeled through various agencies. The Ministry of Construction's headquarter establishment is weak and is not organized according to its main functions, one of which is highways. Road maintenance, which is insufficient and of poor quality, is the responsibility of Provincial Governments, under the Ministry of Home Affairs, while the Ministry of Construction has only an ineffective advisory role. The studies to be made will review the present highway administration and formulate recommendations for improvements.

12. On the basis of the recommendations resulting from the consultants' studies a national administration for public roads and an organization for transport coordination would be established in accordance with a program agreed between the Government and the Association. The proposed credit would provide for financial assistance in setting up these organizations and for training overseas of Korean personnel in highway engineering and administration and in transport economics.

13. The project would be carried out with the assistance of three consulting firms. One firm would study and make recommendations on highway organization and transport coordination, and two firms would do feasibility studies on different segments of the roads. At a later stage in the project contracts will be negotiated for detailed engineering of selected roads.

14. The proposed credit would be for a term of twelve years, including a grace period of four years. The long grace period is required to accommodate the detailed engineering studies and the fellowships for overseas training. The Association would have the right to require the Government to prepay this credit out of the proceeds of any Bank loan or IDA credit made for the purpose of constructing the roads to be engineered under this project.

PART IV - LEGAL INSTRUMENTS AND AUTHORITY

15. The draft Development Credit Agreement between the Republic of Korea and the Association and the Recommendation of the Committee to be provided for in Article V, Section 1(d) of the Articles of Agreement are being distributed to the Executive Directors separately. The draft Development Credit Agreement generally follows the pattern of Development Credit Agreements for pre-investment projects.

PART V - THE ECONOMY

16. A report entitled "Current Economic Position and Prospects of Korea" (AS-133), dated January 11, 1968, in four volumes, was distributed to the Executive Directors: Volume I (the Main Report) on January 16, 1968 and Volumes II-IV are available upon request. The report noted that Korea's recent economic performance has been impressive. GNP growth in real terms accelerated from 7 percent per annum in 1962-64 to over 10 percent in 1965-66. The rate fell to 8.4 percent in 1967 because of a severe drought.

17. Manufacturing is the most significant fast-growing sector, with growth rates increasing from 12 percent per annum in 1962-64 to over 20 percent in 1965-67. Export expansion is phenomenal; at US\$320 million in 1967, the level of merchandise exports was 3.7 times higher than in 1962-64. Manufacturing exports now account for 70 percent of total exports. The rapid development of manufacturing production and trade is due to the ability of the Korean entrepreneurs, technicians and workers, and the wholehearted support of the Government. The accelerated economic growth has, however, created some bottlenecks in power supply and transport.

18. Gross investment has increased from 13 percent of GNP in 1962-64 to 21 percent in 1967, in an environment of relative political stability and favorable government development policy. A major part of this increase in investment is being financed by increased domestic savings. Improvement in tax collection has contributed to the sharp

increase in public savings from a negligible amount in 1964 to 4 percent of GNP in 1967. Further improvement is expected from the tax reform introduced in late 1967 which may also help in reducing monetary expansion. At the same time, private savings rose continuously to a peak of 11 percent of GNP in 1966, but fell back to slightly below 8 percent in 1967, partly because of the decline in agricultural production and partly because of higher tax payments.

19. Korea's excellent economic performance shows that she is able to put capital to good use. With a still low per capita GNP of US\$155 equivalent the need for importing capital from abroad is likely to continue for a long time to come despite the improved mobilization of domestic resources in recent years. U.S. grant assistance, and low interest long-term loans mainly from the U.S. and Japan, have been supplemented by a large amount of foreign suppliers' credits. The Government gave assurances at the last meeting of the Consultative Group in April that short-term credits will be scrutinized more carefully in the future through making more effective use of the existing control mechanism. However, as the economic report pointed out, even if short-term credits are effectively curtailed the debt service ratio would reach a peak of above 20 percent in 1970 and continue at a level of about 15 percent thereafter. While the country can still stand some additional debt on conventional terms, it is desirable in view of the low level from which development has started and the long period for which the import of capital will be needed that a large part of foreign assistance be on concessional terms.

PART VI - COMPLIANCE WITH ARTICLES OF AGREEMENT

20. I am satisfied that the proposed credit would comply with the Articles of Agreement of the Association.

PART VII - RECOMMENDATION

21. I recommend that the Executive Directors adopt the following resolution:

RESOLUTION NO. IDA

Approval of a Development Credit to the Republic of Korea in an amount equivalent to US\$3,500,000.

RESOLVED:

THAT the Association shall grant a development credit to the Republic of Korea in an amount in various currencies equivalent to three million five hundred thousand United States dollars (US\$3,500,000) to mature on and prior to May 1, 1980, to bear

a service charge at the rate of three-fourths of one percent (3/4 of 1%) per annum, and to be upon such other terms and conditions as shall be substantially in accordance with the terms and conditions set forth in the form of the Development Credit Agreement (Technical Assistance Project - Transport) between the Republic of Korea and the Association, which has been presented to this meeting.

Robert S. McNamara
President

by J. Burke Knapp

Attachment

Washington, D.C.
July 3, 1968